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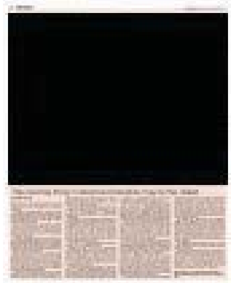

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Inside insights

A decent third quarter

The economy showed marginal improvement in the 3Q23 period as it expanded by 3.3% y-o-y, slightly better than the preceding quarter's growth of 2.9% y-o-y.

AS we come to the tail-end of 2023, the last major market-driven event has just passed on without much enthusiasm as investors probably felt the recently concluded third-quarter (3Q23) reporting season was just a set of another disappointing quarter.

Although the underlying strength of the results was much better than the preceding two quarters, most broking firms are now pushing for even stronger set of earnings growth for 2024, on the back of a lower base this year.

Similar to the 2Q23 and 1Q23 reporting season, some key sectors continued to be weighed down by industry-specific issues as seen in the disappointing performance among plantation and technology companies.

The petrochemicals sector too was a drag. The key sector that saw major earnings surprises was the banking sector with CIMB Group Holdings Bhd, AMMB Holdings Bhd and RHB Bank Bhd reporting better-than-expected quarterly performance.

Selected property and construction names (Sime Darby Property Bhd, IJM Corp Bhd) also provided positive surprises, while the glove sector saw two of the four major players (Kossan Rubber Industries Bhd and Hartalega Holdings Bhd) posting a quarterly profit for the first time in a year.

In the aviation sector, both AirAsia X Bhd and Capital A Bhd reported core losses, mainly due to higher fuel costs.

Major earnings surprises this time around were from poultry breeders like Leong Hup Holdings Bhd and Teo Seng Capital Bhd, which reported spectacular earnings jumps.

In the utility sector, Tenaga Nasional Bhd and Malakoff Bhd saw poor performances. The same of course cannot be said of both YTL Corp Bhd and YTL Power International Bhd, which saw significant year-on-year (y-o-y) gains in revenue and earnings for their 1Q23 reporting period, while in the healthcare sector, IHH Healthcare Bhd's 3Q23 results were surprisingly strong.

The automotive sector too continued to benefit from pent-up market demand as companies like Bermaz Auto Bhd, MBM Resources Bhd and UMW Holdings Bhd reported strong earnings growth, but Tan Chong Motor Holdings Bhd remained in the red as the company's vehicle range saw low demand and was uncompetitive.

Gaming companies too showed promising results during the quarter, while consumer names were mixed.

Drop in nominal GDP

The economy showed marginal improvement in the 3Q23 period as it expanded by 3.3% y-o-y, slightly better than the preceding quarter's growth of 2.9% y-o-y.

Interestingly, the quarterly trend improved further as the 3Q23 gross domestic product (GDP) growth of 2.6% on a quarter-on-quarter (q-o-q) seasonal-adjusted basis was stronger than the preceding quarter's growth of 1.5%, and the 1Q23 growth of just 0.9%.

In nominal terms, the Malaysian economy expanded 5.3% q-o-q to RM462.7bil in 3Q23. The positive economic momentum compared with the preceding quarter was also mirrored by corporate Malaysia as net earnings expanded 8.7% q-o-q.

Compared to a year ago, while the economy grew 1.2%, corporate earnings expanded 2.6% for the same period. The positive earnings momentum augurs well for the growth outlook going into 2024.

Improved performance

As analyst expectations were expected to be more accurate for 3Q23 than the preceding two quarters as they have the benefit of actual results for the first half of the year, it was not surprising to see a much-improved set of results.

The ratio of companies' earnings that surprised the market against those that were below expectations improved as 22.5% of companies reported earnings that were above expectations against 32% that were below consensus estimates.

This was slightly firmer than the preceding 2Q23 and 1Q23 reporting seasons when 14.2% and 11.4% of companies reported results that were above expectations and 34.5% and 37.6% were below expectations, respectively.

Hence, the earnings disappointment ratio improved to 1.43 times from 2.43 times and 3.31 times in 2Q23 and 1Q23, respectively.

Firmer growth in 2024

Following the 3Q23 results, there have been some adjustments to earnings estimates for 2023 as well as for 2024 growth expectations.

For 2023, from the earlier forecasted earnings growth of just 0.4% at the end of the 2Q23 quarterly reporting period, the revised estimate now shows negative earnings of 0.2% for this year, a drop of 0.6 percentage points.

Earnings for 2024 are now estimated to grow 13.5% y-o-y from the earlier estimate of 11.8% growth, an increase of 1.7 percentage points.

While the earnings forecast for 2023 is largely discounted by the market for now, it is rather worrying to see growth expectations for 2024 have been rising at a rapid pace. This could lead to higher market valuations for the benchmark FBM KLCI, but only on the assumption that this expectation is met.

Time and again, we have seen how bullish earnings forecast over the next financial year can be at the tail-end preceding year, but only to be disappointed along the way as corporate Malaysia seems to be good at not meeting expectations.

Window dressing

As the FBM KLCI is 3.6% lower than its 2022 year-end close of 1,495 points, and we are just two weeks away from the year-end, the consensus estimate is still looking for the index to end the year with a bang with an average year-end target of 1,505 points – a good 4.3% upside from Thursday's close of 1,442.85 points.

While the upside in terms of index level may not be significant, one cannot discount the possibility of window-dressing activities taking place.

Among the key index stocks, which have been battered down the most, Axiata Group Bhd looks like a prime candidate for a window dressing push towards its last year's close of RM3.09, a potential 30.9% upside from Thursday's close of RM2.36.

There is also a likelihood of a re-rating for Axiata, given the company's move to sell its Nepalese business operations via NCell Axiata.

Other worthy candidates with more than 20% upside are MR DIY Group Bhd, PPB Group Bhd, Nestle (M) Bhd, and PETRONAS Chemicals Group Bhd, with a potential upside of between 23% and 28%.

Eventful year ahead

Several key events will drive market sentiment next year and this will be further explored in the upcoming final two columns over the Christmas and New Year weekend.

Broadly, the year will not only be dictated by where the US interest rates and liquidity are heading but also by geopolitical risks, including several key general elections taking place globally, that could take a different turn altogether.

Domestically, few events will likely dictate market direction other than the expected reform measures that the capital market is looking forward to.

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